

Manhattan Office Market Q1 2020 Topics and Trends

While Manhattan remains a premier global investment market, its performance in the year ending Q1 2020 indicates that sales volume in the Class A and B office market is down considerably compared to recent years and fundamentals are currently being heavily watched as the current COVID-19 crisis develops. Total dollar volume in the year ending Q1 2020 is down 42% from year ending Q1 2016 with decreases seen year over year. This report analyzes the trends in market fundamentals and investment sales in the Manhattan Class A and B office market, including the Midtown, Midtown South, and Downtown submarkets.

FEATURE: COVID-19 and its Impact on the Market

In Mid-March 2020, the Global COVID-19 Pandemic brought much of the world and New York City to a halt. The spread of the virus was so rapid, that nations, states and local municipalities were forced to take drastic measures. In addition to the health risk itself, there is ongoing societal angst with most US citizens living under state mandated lockdown orders. Further impacting the economy is that the lockdown orders involve closing down businesses that are considered non-essential.

For the commercial real estate market segment, this crisis will have both short-term impacts that are now becoming obvious. It will also have long-term impacts that will unfold over time.

Short Term Impact

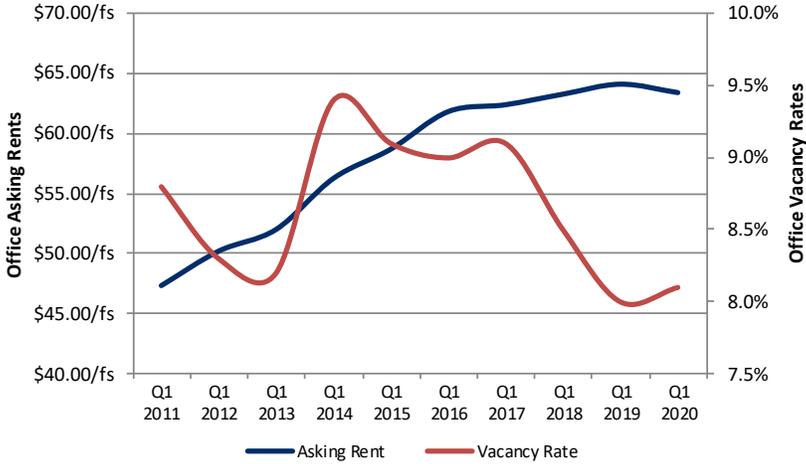
Due to the nature of COVID-19, the state of New York, along with most other states, mandated a lockdown that encourages all people to stay home. Businesses have been classified as either non-essential, in which case the business must close, or essential, in which case it can stay open. Even the construction industry has been shuttered.

Closures have displaced thousands of workers. With business closures, and with thousands unemployed or furloughed, there is an immediate concern about how tenants will be able to continue paying rent.

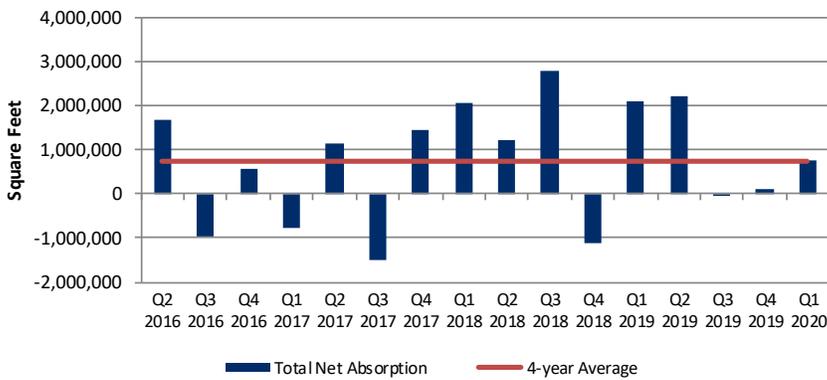
Long Term Impact

The impact of COVID-19 on commercial real estate is going to unfold over time. With most non-essential workers growing accustomed to working from home full time, there are questions surrounding the need for traditional office space once businesses re-open. Most likely, the ideas of co-working space and open floor plans that were growing pre-pandemic, will dissipate.

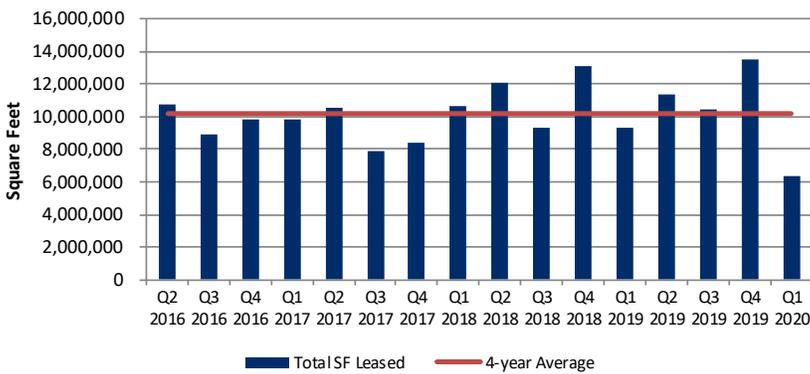
Asking Rents and Vacancy Rates



Total Net Absorption



Total SF Leased



Space Additions



MARKET FUNDAMENTALS: Average Asking Rents & Vacancy

Prior to the pandemic, fundamentals were healthy. Between Q1 2011 and Q1 2020, vacancy rates fluctuated between a low of 8.0% (Q1 2019) and a high of 9.4% (Q1 2014). Over the past year, vacancy rates increased nominally. Asking rents were increasing relatively consistently up until the most recent quarter, ranging from \$47.36 per square foot (Q1 2011) to \$64.11 per square foot (Q1 2019), but decreasing slightly in Q1 2020. If the pandemic causes an extended dip in demand, vacancies will likely rise, and rents will flatten or decline. We are likely heading into a tenant’s market.

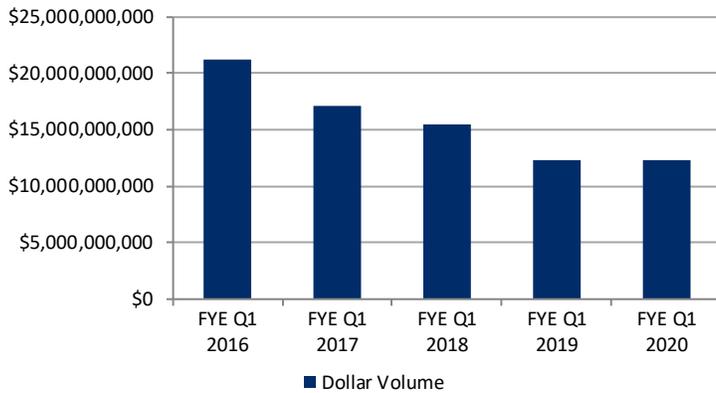
Net Absorption and Leasing Activity

Total net absorption in the Manhattan market has been relatively low since the end of 2019 but is trending upwards, indicating a potential increase in net absorption. Total square feet leased has fluctuated recently but Q1 2020 shows a significant drop from the leasing activity seen in 2018 and 2019. It is expected that COVID-19 will cause a lag in leasing activity as building tours are cancelled and employees grow accustomed to working from home, limiting the demand for traditional space.

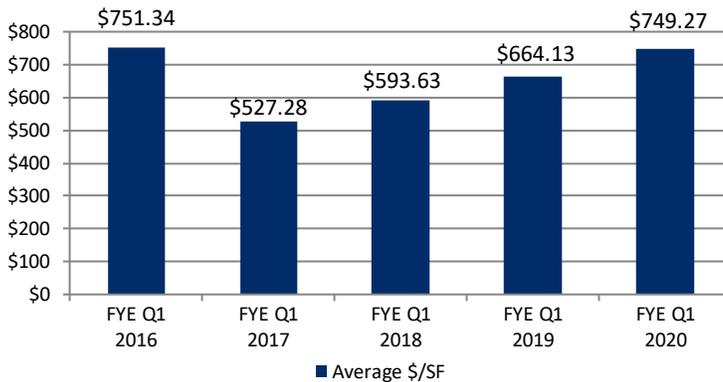
Space Addition Activity

There is still a fairly large amount of space under construction that is waiting to be delivered, indicating an active construction pipeline prior to the pandemic outbreak. With increased transit connectivity, tenants have shifted their focus from just the Midtown core and are now open to different areas of the metro, like Hudson Yards. Although currently halted, construction activity is expected to resume as developers recognize the shifting focus from the midtown core and meet the demands of the tenants in new areas.

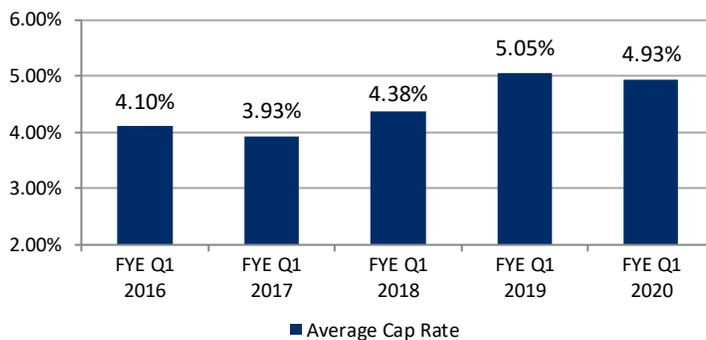
MANHATTAN OFFICE BUILDING DOLLAR VOLUME



MANHATTAN OFFICE BUILDING AVERAGE \$/SF



MANHATTAN OFFICE BUILDING AVERAGE CAP RATE



SALES (5 YEAR TREND): Volume

Total dollar volume for investment sales of Class A and B office buildings in Manhattan has been decreasing year over year since the beginning of the analysis period. Since 2016, when a surge of Chinese investment capital flowed into the metro, there has been a significant decrease in total dollar volume, down to \$12.3 billion in 2019 compared to \$21.2 billion in 2016. The 2020 results are 42% lower than 2016 but on par with 2019.

Average Pricing Per SF

There was a significant increase in average pricing in the last year. The average as of 2020 was \$749.27 per square foot, which is a 13% increase compared to the pricing seen in 2019. Market participants will be watching this metric carefully for the remainder of 2020.

Capitalization Rates

The average cap rate for Class A and B office buildings in Manhattan decreased slightly in the last year. As of a Q1 2020 report, PwC placed this market in expansion through 2020, moving into contraction for 2021 and recession for 2022 and 2023; however, this timeline has already been shifted due to COVID-19. Deal making is at a standstill due to COVID-19; however, landlords may choose to wait before they drop their asking prices, which means cap rates and pricing could remain stable in the short term.

SOURCE: CoStar and Marshall & Stevens



Patrick T. Craig, MAI, MRICS
Executive Managing Director
Real Estate Valuation Practice
212.897.9481
ptcraig@marshall-stevens.com



Emily Ferreira
Senior Associate
Real Estate Valuation Practice
646.438.7605
eferreira@marshall-stevens.com



Jacob Scott
Analyst
Real Estate Valuation Practice
646.438.7606
jscott@marshall-stevens.com